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Penetrative Pricing: Understanding its Evolution and Rationale Under the Indian Competition Law Regime Through the Revolutionary Jio Case

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Jio's Onslaught of the Indian Telecommunication Market

On 5th September, 2016 Reliance Jio Infocomm Limited(RJIL) (hereinafter referred as 'Jio') released its free data and voice scheme 'Jio welcome offer' which was further extended till December. Next, it introduced 'Happy new year offer' which extended the previous plan till 31 March, 2017. Even in 2018 and now in 2019, it is charging nominal rates to provide high speed data and voice which instigated the Indian digital revolution. For the first time in India, humongous investments were done and a new entrant penetrated the telecommunication market which was held tightly by few incumbents.

They successfully penetrated the market within a year. However, their zero pricing strategy was declared predatory and anti-competitive. They were on thin ice, where a single characterization of dominance demarcated them from being penalized for anti-competitive behavior. This portrays the beginning of a new era for Indian competition law, where a revolutionary pricing strategy was applied which provided the consumers utopian incentives. The spotlight of our attention should be focused on a particular phase 'penetration' and its relation and position with Indian Competition Law. It remains a gray area and has demonstrated potential to renovate the competition law scenario in India.

Controversial Pro-Penetration Stand of TRAI

An interesting perspective can be extracted from Telecom Regulatory Authority of India's (TRAI's) ruling concerning the predatory price allegation on Jio. Jio made its mark on the telecommunication market when it started providing free data and voice services in 2016. Consequently it generated a gargantuan shift in the consumer base. Even when they started charging for their services, it was still a fraction of what its rivals (Airtel, Vodafone and Idea) were charging. In 2018, TRAI amended the predatory pricing rule which caused a disruption in the market, especially for the rivals of Jio. It permitted Jio to continue with its low pricing but barred its rivals to reduce their current prices to tackle competition. It reasoned that the rivals' existing position would cause abuse, whereas, Jio being a new entrant was inept to abuse (predation). It also scrapped traffic volume as a parameter for establishing market power, which gave absolute

immunity to Jio, as it was experiencing huge growth in terms of traffic volume. However, these changes were nullified by the sectoral appellate tribunal, when the rivals challenged them on the merits of intent and capability of Jio. The sectoral appellate tribunal observed that TRAI's changes offered 'artificial protection' to the entrant and as a counter-measure allowed the rivals to offer cheap rates to compete with the low tariffs of Jio. Two polar views can be observed here, while TRAI directly allowed penetrative pricing as it granted the relaxations to Jio due to its nascent position , the appellate tribunal rejected the merit of market penetration through low pricing, thereby rejecting the theory of penetrative pricing by ignoring the entrant's position and denying it the benefit of newcomer's promotional pricing opportunity.

Penetrative Pricing: The Search for Clarity and Dawn of its Undeniable Existence

Unlike predatory pricing, penetrative pricing is not much popular in the arena of competition law. Competition Act, 2002(hereinafter the 'Act') which regulates competition in India is silent upon this matter to the extent where there is no explicit mention about it in the entire Act. Certain topics regarding penetrative pricing are discussed below in an attempt to clear the fog:

1. Definition- Penetrative Pricing is a common marketing and pricing strategy. Seldom has a clear and concise definition been provided in the cases or the regulating bodies which encompasses majority of the aspects of penetrative pricing with respect to competition law. A hypothetical definition is being provided here:

'*Penetrative pricing can be defined as lowering (usually) of prices of items or services by an non-dominant entrant entity to establish, promote and highlight its identity and existence in the market, where multiple incumbent players already exist , with the anticipation, preparation and objective to expeditiously attract the consumers' attention at the expense of suffering initial losses which may or may not be recouped once their identity is established through this short term incentive-based strategy.*'

The term penetrative price was predominantly used in the *National Stock Exchange of India Ltd. & DotEx International Ltd. v. MCX Stock Exchange* (hereinafter '*NSE Case*'), and then in *Fast Track Call Cab Pvt. Ltd & Meeru Travel Solutions Pvt. Ltd. Vs. ANI Technologies Pvt. Case*(hereinafter '*cab case*'). However, the former was rejected on grounds of anti-competitiveness, abuse of dominance and intention of predation, while in the later they didn't venture into the legitimacy of the pricing strategy i.e., the concept of penetrative pricing, but approved its logical and circumstantial foundation making it critical to note that they cited non-dominance and not pro-competitiveness of penetrative pricing for letting it continue its practice which doesnot confirm their view on this strategy.

It was first successfully applied and accepted by Competition Commission of India (CCI) in *Bharti Airtel Ltd. v. Reliance Jio Industries Ltd.*(hereinafter '*Jio case*'). It was also the first instance where they appreciated its strategic value and provided certain criterions, however, these were included in the obiter dicta portion and not in the ratio decidendi one, which illustrates that it is yet not prepared to formally accept it as a pro-competitive and major strategic development in the Indian competition law sector. This makes it ambiguous in nature as the opinion of the commission remains unclear as it did not set formal guidelines, keeping it open to future

interpretations.

2. Nature- The very essence of penetration is to increase market diversity and offer better choices to the consumers which can be termed as pro-competitive in nature.

The underlying principle of penetrative pricing was implied by the CCI in the *cab case* as: 'A new entrant armed with new idea, superior technology or a superior product or technological solution that challenges the status quo in a market and shifts a large consumer base in its favour would cannot always be as held dominant'. This establishes the pro-competitive nature of penetrative pricing which can be wrongly portrayed as predatory price with mala fide intention aimed at anti-competitiveness.

This article provides a similar observation: "*predatory pricing is a convenient weapon for businesses that do not want to match their competitors' price cutting. Filing an antitrust lawsuit is a common alternative to competing by cutting prices or improving product quality, or both.*"

A unique feature of the *Jio case* is its initial zero pricing strategy. It was nefariously used in the *NSE case*, but NSE being the dominant entity was not considered under the ambit of penetrative price but was rather monopolistic in nature. However, in the *Jio case* it was successfully accepted by the commission on the grounds that Jio was an entrant. Nonetheless, certain pertinent questions remain debatable as to the time period of this strategy, its intent, its position as to the pricing factor and its implication in causing temporary disruption of the status quo. In *Jio case*, zero pricing drove the entire focus on the quality which the consumers had the free choice to test and compare. While zero prices tend to prevent firms from competing on price, they invite competition on quality. Entrants can produce greater quality at zero prices and suffer losses temporarily, if they are superior they will gain market share in the future and recoup the losses. It debunks the theory which tags zero pricing as an anti-competitive dead end in competition law.

3. Criteria- The CCI hinted at certain criterions as observed in the *Jio case*. They include non-dominant nature of the offering company, intent of incentivization, absence of competition reducing approach and its short time span. The Commission expressed its opinion as follows:

"*providing free services cannot by itself raise competition concerns unless the same is offered by a dominant enterprise and shown to be tainted with an anti-competitive objective of excluding competition/ competitors, which does not seem to be the case in the instant matter as the relevant market is characterised by the presence of entrenched players with sustained business presence and financial strength. In a competitive market scenario, where there are already big players operating in the market, it would not be anticompetitive for an entrant to incentivise customers towards its own services by giving attractive offers and schemes. Such short-term business strategy of an entrant to penetrate the market and establish its identity cannot be considered to be anti-competitive in nature and as such cannot be a subject matter of investigation under the Act.*"

It differs from the *cab case* from a fundamental viewpoint. In these cases, they came to notice mainly due to their convenience and relatively low pricing, whereas, the opposite happened for Jio. Its zero pricing garnered public attention where quality took the secondary pedestal, however, upon trial the consumers found its quality to be peerless in the whole country. These two factors

spearheaded Jio's telecommunication crusade.

Predation: Dissecting the Infamous Allegation

It is imperative to understand predation in order to establish its relation, effect and influence on penetration. Predatory price finds its mention in Section 4(2)(a)(ii) of the Act and is elaborated in the explanation as:

''predatory price' means the sale of goods or provision of services, at a. price which is below the cost, as may be determined by regulations, of production of the goods or provision of services, with a view to reduce competition or eliminate the competitors.'

Thus the rivals in the market are unable to compete with the price of the dominant player and will have to leave the market or endure losses which are terminal in nature. The CCI in *Re: Johnson And Johnson Ltd.* held that "the essence of predatory pricing is pricing below one's cost with a view to eliminating a rival."

Predatory pricing is considered as a severe form of dominance. It is considered as an anti-competitive offence in most nations' competition regulation principles. Previously Article 82 of the Treaty establishing the European Community(TEU) used to regulate and prohibit it[1]. In USA, Section 2 of the Clayton Act[2] prohibits predatory pricing.

There exists various tests which predict the predatory nature of a company pricing policy. Here, a brief discussion is provided in order to understand the relationship between predation and penetration.

The Two Pillars of Predation: Intention and Recoupment

The present is dictated by the past and forms a foundation for the future. To understand any present competitive move we must track its past and predict its future moves to understand it exhaustively. Intention and recoupment are the two pillars for tests of predation.

In *M/s. Transparent Energy Systems Pvt. Ltd. v. TECPRO Systems Ltd*. the Commission held the following three condition for identification of predation:

1. The prices of the goods or services of the dominant firm are below the cost of production of such goods or acquisition of such service.
2. Such decline in the prices of the dominant firm was brought with the intention of driving the competitors out of the market.
3. There is a significant planning in order to recover or recoup the losses that are incurred by increasing the prices again after the competitors are forced out of the market.

In the *NSE case*, a similar principle was followed. The last two criterions were laid down as a two prong test. However, the European perspective differs largely. The Court of Justice of the European Union(CJEU) in the *Wanadoo case*[3] argued that '*demonstrating that it is possible to recoup losses is not a necessary precondition for a finding of predatory pricing*'. This established a

presumption of predation on below Average Variable Cost(AVC) prices without any satisfactory demonstration. It makes the predation prediction fragile as it ignores the intention which essentially results in ignoring the purpose of the move. If the objective of an act remains unknown and is not considered, future predictions become prone to misjudgements and errors. Similar observation was made by the Court of First Instance in *Tetra Pak II case*[4] as well as in the *France Telecommunications Case*.

However, in *Compagnie Maritime Belge case* Attorney General Fenelly[5] presented his contrary view that recoupment should be part of the test for predatory pricing. In the *AKZO* case, the European Court of Justice(ECJ) linked intent with recoupment and subtly accepted the criteria of recoupment:

"*A dominant undertaking has no interest in applying such prices except that of eliminating competitors so that it can allow subsequently raise their prices by taking advantage of their monopoly position since each sale generates a loss*".

The court of justice usually considers four points while testing for predation which are dominance, price, intention and recoupment. However, it is open to accept such activities under the exception of objective justification

With regard to the *Jio case* the four factors stand as follows:

1. Dominance- When the penetration pricing strategy was applied it was not a dominant entity, rather its rivals were close to holding dominant positions.
2. Price- this factor remains foggy as to where exactly Jio's zero pricing policy would stand in the price test.
3. Intention-the intention was to penetrate the market which maybe confused with predation, but owing to its nascent nature, presumption for penetration seems apparent.
4. Recoupment- this factor which characterizes every predation, was not observed in Jio's case. Even after penetrating the market it charged minimal rates which entirely punctured the allegation of recoupment.

Thus, it can be observed that Jio's strategy doesnot come under the scope of predation per se but essentially constitutes an indispensable technique which favours competition.

Retrospective Analysis of the Rivals' Allegations with Reference to the Competition Act, 2002

It is interesting to note that the rivals who alleged jio to practice Anti-competitive activities and cause Appreciable Adverse Effect on Competition(AAEC), would themselves be violating section 4(b)(ii)[6] and section 19(3)(f)[7] of the Act as they both prohibit restrictions on promotion or development of scientific, economic and technical provisions , if their long lived monopolistic attitude and consistently high rates with negligible advancement in any form is considered. The digital revolution that was catalysed by Jio was mainly due to scientific developments and investments. The reasons behind Jio's success are as follows:

"*In 2010, Mukesh Ambani bought 96 percent stake in Infotel Broadband which had won 4G spectrum in all sectors in India. Later they renamed it to Jio, and started building fibre optic network around the country*". Opposing capital investment in the market would mean to

obstruct[8] the flow of capital which would invariably resist the technological advancement as well.

Fibre Optic network and towers offer higher data capacities to the consumers. A 2,50,000 kilometres route of fibre optic cables and 90,000 eco-friendly 4G towers are in process to transform India's digital scenario. The zero pricing and unlimited free services were feasible because data providers have limited data as they donot possess enough capacity (bandwith) to administer large amounts of data. While due to Jio's huge fibre optic transformation this regressive threshold is being crossed. The rivals have never cared to invest in optic fibres. They pay other companies to use their optic fibres which increase the charges, while Jio can safely eliminate the same charge and therefore, reduce prices. The bubble of technological backwardness and lack of investment upon rupturing has created massive delusionary response from the rivals who oppose this technological advancement due to their entrenched ignorance. Prohibiting Jio's service would mean serious denial of benefits to consumers who have until now paid for geriatric, outdated and less efficient technologies. Thus, the challenges posed by the rivals suffer from anti-competitiveness veiled under the disguise of protectionist provisions of the Act.

Long Live the Customers?

The ultimate trial stands on the competitiveness of penetrating price. The creation of competition regulations around the globe had certain specific purposes. Maximum Consumer welfare holds paramount interest in these acts. To put it simply, if all other aspects of penetration were to be ignored, and only the strongest argument remains i.e., effect on the consumers would be the litmus test. Consumers are benefited to the maximum extent when there is race for low price and high quality. It can be argued that the regulations attempt to portray a consumer first policy. The preamble[9] of Competition Act mentions protection of consumer interest. In *CCI v. SAIL**[10]*** it was reiterated by the Supreme Court of India that: 'The main objective of competition law is to promote economic efficiency using competition as one of the means of assisting the creation of market responsive to consumer preferences'. Jio's penetration pricing strategy qualifies as productive, allocative and dynamic wise efficient as mentioned in the act. In *Österreichische Postsparkasse AG*[11] and *GlaxoSmithKline**[12]** cases*, the General Court held the welfare of the consumers as the main goal of competition law.

Article 102 of the Treaty on the Functioning of the European Union(TFEU) places welfare of the consumers at a higher pedestal than preservation of the competitors' equilibrium. It enshrines various pro-consumer provisions under its objective justification requirements such as allowance of alleged anti-competitive or dominant behaviour which outweighs the anti-competitiveness and gives the consumers substantial benefits and accelerated efficiency which largely counters the claims of the incumbent and rivals who are inclined towards protecting their regressive status quo over consumer welfare.

The President of the General Court claimed that, "*the primary purpose of Article 102 is to prevent the distortion of competition, and, especially, to safeguard the interests of consumers rather than simply protect the position of particular competitors**[13]***"

Call for Guidelines: Wake Up Call for the Slothful CCI?

It can be concluded that the strongest argument for penetration remains its pro-consumer behaviour which reaches its maximum value under zero or reduced pricing. However, with reference to the Indian Competition law regime, there is a dire need for regulation of this unique pricing strategy in the form of guidelines or amendments in the Act to specifically define the term and provide the criterions and the restrictions. Such extreme strategy is equally potential to harm the consumers with future monopolistic behaviour shrouded under the veil of temporary pro-consumer and consumer first policy through heavy recoupment. As per the *Jio case*, no such behaviour has yet been observed. It continues its dirt cheap charges and remains the torchbearer for digital revolution in India. It also sheds positive values and expectations from the application of penetrative pricing in Indian competition law regime. It must be noted that Indian competition law is still in a phase of evolution and infancy unlike its European or American counter-part and remains open to speculations coupled with further behavioural observations regarding the use of this unique pricing strategy.

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[1] Communication from the Commission — Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings

[2] Clayton Act, 1914

[3] Case C-202/07 P France Télécom SA v Commission of the European Communities (2009) ECLI:EU:C:2009:214, para 113.

[4] wanadoo teCase C-333/94 P Tetra Pak International SA v Commission of the European Communities ECLI:EU:C:1996:436.

[5] Compagnie Maritime Belge SA (C-395/96 P), Opinion of Advocate General Fennelly ,1998

[6] Competition Act, 2002 Section 4 (b) limits or restricts:

(ii) technical or scientific development relating to goods or services to the prejudice of consumers;

[7] Competition Act, 2002 , Section 19 3 (f) promotion of technical, scientific and economic development by means of production or distribution of goods or provision of services.

[8] Avtar Singh, 'Competition Law' (1st Ed. Eastern Book Company(EBC) 2012), Page 90

[9] Competition Act, 2002: Preamble "*An Act to provide, keeping in view of the economic development of the country, for the establishment of a Commission to prevent practices having adverse effect on competition, to promote and sustain competition in markets, to protect the interests of consumers and to ensure freedom of trade carried on by other participants in markets, in India, and for matters connected therewith or incidental thereto*"

[10] CCI v. Steel Authority of India(SAIL): "*As far as the objectives of competition laws are concerned, they vary from country to country and even within a country they seem to change and evolve over the time. However, it will be useful to refer to some of the common objectives of competition law. The main objective of competition law is to promote economic efficiency using competition as one of the means of assisting the creation of market responsive to consumer*

preferences. The advantages of perfect competition are threefold: allocative efficiency, which ensures the effective allocation of resources, productive efficiency, which ensures that costs of production are kept at a minimum and dynamic efficiency, which promotes innovative practices. These factors by and large have been accepted all over the world as the guiding principles for effective implementation of competition law."

[11] Österreichische Postsparkasse AG and Bank für Arbeit und Wirtschaft AG v. Commission of the European Communities, Joined cases T-231/01 and T-214/01 [2006], para. 115

[12] GlaxoSmithKline Services Unlimited v. Commission of the European Communities, Case T-168/01 [2006], para. 171

[13] IMS Health Inc., v. Commission of the European Communities, T-184/01 R, Order of the President of the Court of First Instance [2001], para. 145.

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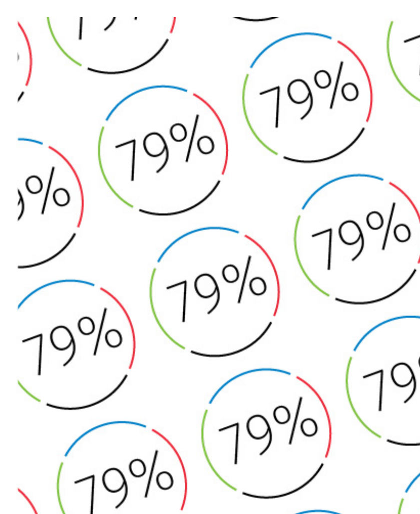

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